

2008 COMPETITIVE BID HEARINGS

Findings and Recommended Rental Rates for
Agricultural and Grazing Lease Nos.
9701 and 3121

A report to the State Board of Land Commissioners by
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On May 1, 2008 the Department held Competitive Bid Hearings for State of Montana Agricultural and Grazing Leases Nos. 9701 and 3121, which are under review for renewal in 2008. These new ten-year leases will expire on February 28, 2018. If a Lessee wishes to renew the lease for another term he must submit an application. If other persons inquire about the availability of a lease, their names and addresses are noted in the file and they are sent applications and bid forms at the time of lease renewal.

The statutory absolute preference right within Section 77-6-205(2), MCA, to renew a State agricultural and grazing lease was declared unconstitutional by Judge Jeffrey Sherlock in Broadbent v. State of Montana, et al., First Mont. Judic. Distr. Ct., Cause No. BDV-2003-361, because it impermissibly interfered with the constitutional power of the Land Board, under Art. X, Section 4 of the Montana Constitution, to choose its lessees. The Land Board, in response to Judge Sherlock's ruling, amended ARM 36.25.117 to exercise its constitutional prerogative to grant a qualified preference right to incumbent lessees in good standing. Through this rule, the Land Board has expressed its qualified preference to issue renewals of agricultural and grazing leases to the incumbent lessee provided that they have not committed illegal subleasing and do not have a history of lease violations. However, in all instances, the Board has reserved the right to choose the best-qualified lessee.

As part of its constitutional power, the Land Board may also determine the rate at which such leases will be issued. The Land Board has recognized that full market value encompasses the concept of sustained yield. Section 77-6-101 MCA. In Jerke v. State Dept. of Lands, 182 Mont. 294, at 296-297, 597 P.2d 49 at 50-51 (1979), the Montana Supreme Court held that a Grazing District which was not a lessee of a state grazing lease could not exercise a preference right. The Court described the rationale of the preference right to meet a high bid as follows:

Sustained yield is the policy which favors the long term productivity of the land over the short term return of income. State ex rel. Thompson v. Babcock, supra. The preference right seeks to further this policy by inducing the State's lessees to follow good agricultural practices and make improvements on the land. This is accomplished by guaranteeing that the lessees will not lose the benefits of their endeavors by being outbid when their leases terminate. They are preferred and may renew their leases by meeting the highest bid submitted.

Id.

Exercised in such a manner, such a preference may be in the best financial interests of the school trust beneficiaries. All other things being equal, the Land Board has recognized that stability of land tenure encourages existing lessees to make greater improvements in the land, knowing that they will likely be able to utilize these improvements in the future, and that stability of tenure allows lessees to operate more efficiently. The duty to maximize revenue return to the trust estate from the trust properties is always subject to the duty to preserve the financial productivity of the trust lands. Oklahoma Education Association v. Nigh, 642 P.2d 230 at 238 (1982)

No Applicant for a grazing lease can compel the State Board of Land Commissioners to grant it an interest in state trust lands, especially where the concept of sustained yield is ignored. See, Skillman v. Department of State Lands, 188 Mont. 383, 613 P.2d 1389 (1980); Gibson v. Stewart, 50 Mont. 404, 147 P. 276 (1915)(Whether a tract of state land shall be leased is a

question addressed to the sole discretion of the Land Board.); §77-6-206, MCA ([T]he board may withdraw any agricultural or grazing land from further leasing for such period as the board determines to be in the best interest of the state”).)

Under ARM 36.25.117, if the Lessee exercises the qualified preference right but believes that the bid amount is excessive, he or she may request a hearing. The purpose of the hearing is twofold: 1) to determine the best-qualified Lessee for the upcoming lease term; and 2) to ascertain the appropriate rental rate for that term. Specifically, the Director inquires whether the high bid amount represents the fair market value of the lease and whether the rental rate is truly in the best interests of the trust. In determining whether the "high bid" rental rate is in the best interests of the beneficiaries of the trust, the Land Board must utilize the criteria set out in §77-6-205(2), MCA, and in Thompson v. Babcock, 147 Mont. 46, 409 P.2d 808 (1966). Under these criteria, the Montana Supreme Court has held that the "high bid" may be rejected where it is either "...above community standards for a lease of such land, would cause damage to the tract, or impair its long-term productivity".

The Montana Supreme Court has recognized that an excessive rental rate, at some point, economically compels a Lessee to graze all the available forage on a grazing lease or reduce costly fertilizer, herbicide, and summer fallow treatments on agricultural leases. When state lands are over-grazed or farmed with minimal input costs, they produce more noxious weeds, less forage or crops, and less future income for the beneficiaries of the various trust lands. In extreme cases, the productivity of the land may be permanently damaged. It is in the best interests of the State to set a rental rate which balances the competing factors. In this "balancing act", the Land Board is attempting to maximize long-term income by allowing the Lessee a sufficient monetary incentive to exercise wise range management and agricultural practices. If the rate is too low, the State will not receive full market value for its lands. If the rate is too high, the Lessee will be induced to over-graze the tract, or reduce inputs such as herbicides, and long-term trust income will inevitably suffer.

In the competitive bid hearing process, the Director is recommending the rental rate for the next term of the grazing or agricultural lease. The economic viability of these leases fluctuates according to prevailing weather conditions and commodity prices; both of which can vary wildly. Despite these fluctuations, the grazing rental charged by the Board must be paid by the Lessee whether or not any forage upon the lease is utilized. By contrast, private lessors generally do not collect rentals when they no longer have forage available for lease. Consequently, setting an appropriate rental rate, so as to sustain the long-term viability of "school trust" leases and maximize long-term income, is simply not as easy as accepting the highest bid. If it were, there would be no need for a hearing on the subject.

The best lessee is chosen according to nine criteria set out within ARM 36.25.117:

- 1) an intended grazing or cropland management plan for the new term of the lease;
- 2) experience associated with the classified use of the land;
- 3) other non-state lands that are fenced and managed in common with the state land;
- 4) intended grazing or cropland improvements that will benefit the health and productivity of the state lands;
- 5) a weed management plan;
- 6) management goals and objectives and monitoring procedures to determine if they are being met;
- 7) the method or route used to access the state land;

- 8) any other information the director deems necessary in order to provide a recommendation to the board; and,
- 9) the incorporation of all or part of this information as terms and conditions in the new lease agreement.

The current policy of the Board authorizes the Director of the Department to hold the competitive bid hearings; hear the evidence; and make recommendations to the board. Since the rental rates must be based upon the evidence presented at the hearing, the Board members must avoid consideration of information outside the hearing record.

This year the Director granted two requests for hearing. The hearings were conducted on May 1, 2008 at the offices of the Department in Helena, Montana. The hearing was electronically recorded and all witnesses testified under oath. However, the hearings were conducted in an informal manner. Present at the hearings were: Director, Mary Sexton; Trust Lands Management Division Administrator, Tom Schultz; Agriculture and Grazing Management Bureau Chief, Kevin Chappell; Trust Lands Attorney, Tommy Butler; and Land Use Specialists Gary Brandenburg and Craig Biggart.

In preparation for this hearing, both the Lessee and the High Bidder were notified of the time and place of the hearing and given copies of ARM 36.25.117. The High Bidder for Lease No. 9701 appeared and presented testimony to explain the underlying facts and rationale for the High Bid.

When appropriate to the hearing, the Commissioner accepted in the evidentiary record, the following evidence:

GRAZING

1. The Department's County Competitive Grazing Lease Bid Summary for Sweet Grass and Hill County for 2007.
2. The Montana Agricultural Statistics Service Report of Grazing Fee Rates for private leases in Montana reporting an average rate of \$17.80/AUM.

The testimony and evidence considered during the hearing; a summary of the hearing; and the findings and conclusions recommended are set out as follows:

2007 COMPETITIVE BID HEARING

Hearing Time: Thursday, May 1, 2007 at 10:00 a.m.

Lease No.: 9701

Lessee: Jim & Mary Ann Parrent

County: Sweet Grass

Grazing Acres: 159.38 AUM Rating: 42

Ag Acres: 0

High Bidder: J. David Noll

High Bid: \$36.94/AUM

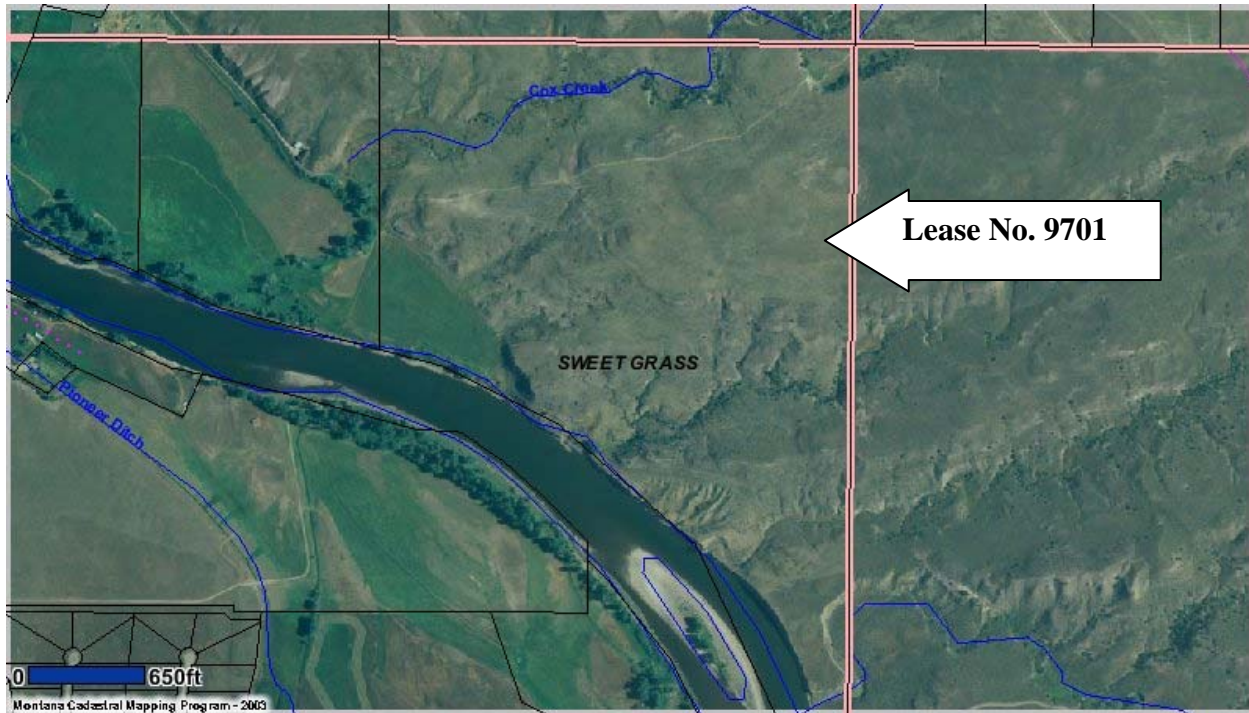
Other Bids: None

Previous Rental: Minimum

Prevalent Community Rental Information:

State Land County Bid Averages: \$14.95/AUM

MT Ag Statistics 2007 Private Lease Rate: \$17.80/AUM



Findings: Mr. Jim Parrent and Ms. Mary Ann Parrent appeared and presented testimony on behalf of the Lessee. Mr. J. David Noll and Ms. Leann Noll appeared and presented testimony on behalf of the High Bidder. This lease is comprised of almost-160 acres of grazing land located largely within NE¹/₄ of Section 16, Township 1 North, Range 5 East, in Sweet Grass County, Montana on the north side of the Yellowstone River. It is approximately 4 miles east of Big Timber, Montana. The Yellowstone River provides an ample source of stock water for this tract. The Lessee accesses this tract through a relative's land, which lies adjacent to this tract. Due to the Lessee's careful stewardship, this tract has seen an astounding improvement in the quality and amount of desirable species of grass. Prior to the tenure of the Lessee, this tract had been abused; and suffered from both over-grazing and a profound infestation of Leafy Spurge. Through the wise and patient application of biological controls and the measured application of herbicide, together with limited grazing, the Lessee has restored the health and productivity of this tract. The lessee has irrigated from 15 to 20 acres of the tract with water pumped from the Yellowstone River utilizing a water right held by the State Board of Land Commissioners. The tract is fenced upon three sides. Although this tract experiences heavy recreational use, the lessee has experienced fewer problems after motorized vehicle use was prohibited. Mr. Parrent believed that the County or State average was a fair rental rate.

The High Bidders, J. David Noll and Leann Noll own a tract of land adjacent to Lease No. 9701 on the Lease's northern border. Mr. Noll stated that he envisioned utilizing Lease No. 9701 as additional pasture for a purebred cattle operation. If he

could obtain additional water, he would like to expand the irrigation on this tract. However, the soil may limit further irrigation of this tract. The upland shale soils on this tract are highly subject to erosion. Mr. Noll related that he didn't need this expanded acreage immediately and would be willing to sublease this tract to the Jim and Mary Ann Parrent for a \$1.00 per year. He would commit to cross-fencing the tract and instituting a rest-rotation grazing program. Mr. Noll stated that he grew up on a farm until age 19, but for the last 43 years, he has engaged in other business. The High Bidders offered no details on any proposed weed management plan. They would access this tract from their private lands to the north.

No evidence was provided in the hearing to show that the High Bid of \$36.94/AUM was either economically or biologically viable for this tract of State land, while adhering to good range management practices.

Recommendation:

I recommend that the Board issue the next ten-year term of Lease No. 9701 to Mary Ann and Jim Parrent at the rate of \$17.80/AUM. The Parrents are the best-qualified Lessee as evidenced by their past management of this tract, and their continuing efforts to control weeds and re-establish grazing forage upon this lease. Given that there are weeds present upon adjacent lands, it will be useful to have an experienced herbicide applicator as a Lessee of this tract. The Lessee's past stewardship of this tract evidences their considerable experience and skill in range management.

This is a desirable tract of grazing land and offers other attributes that may lead to a change in classification in the future. With proper management, this lease can be a prolific source of livestock forage. The Lessee agreed that both the DNRC Sweet Grass County Competitive Bid average and the State-wide Agricultural Statistics rate represented "fair rental rates" for this Lease. Therefore, I find that the state-wide Montana Agricultural Statistics rate for 2007, which is \$17.80/AUM, best reflects the prevailing community standard for this lease.

2007 COMPETITIVE BID HEARING

Hearing Time: Thursday, May 1, 2007 at 11:00 a.m.

Lease No.: 3121

Lessee: Lon & Stacey Waid

County: Hill

Grazing Acres: 640 AUM Rating: 167

Ag Acres: 0

High Bidder: Jeff Solomon

High Bid: \$16.94/AUM

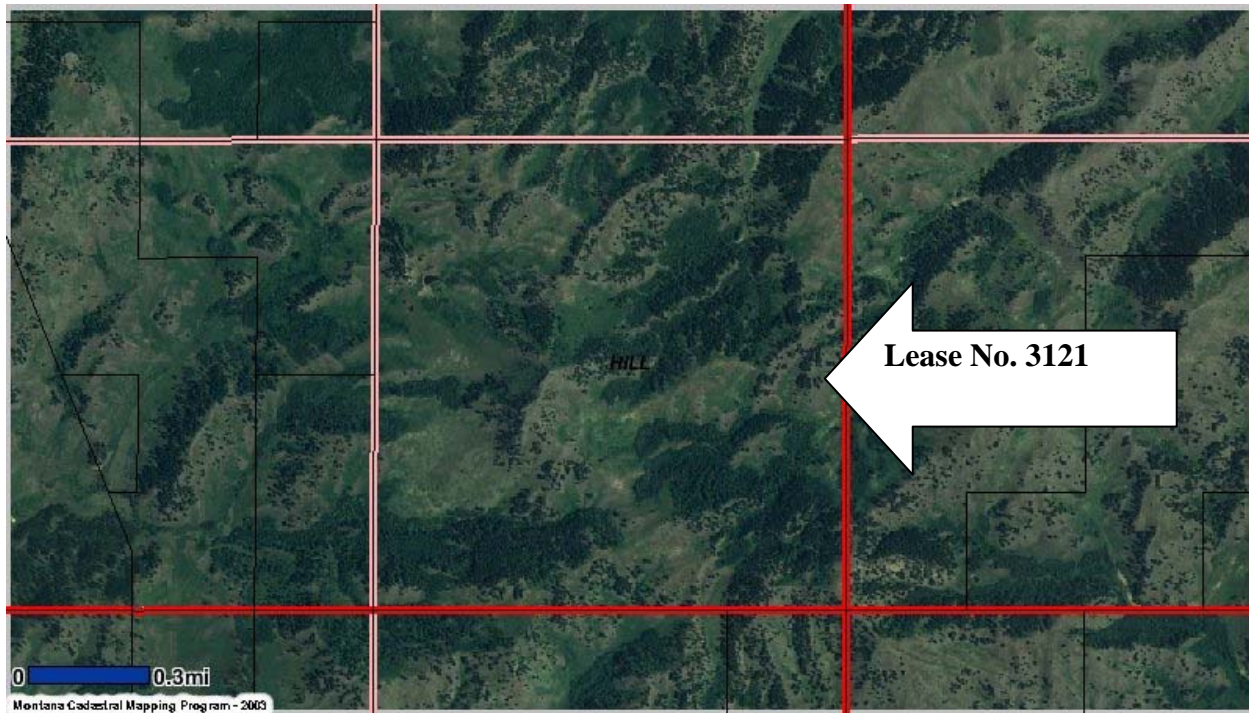
Other Bids: None

Previous Rental: Minimum

Prevalent Community Rental Information:

State Land County Bid Averages: \$10.83/AUM

MT Ag Statistics 2007 Private Lease Rate: \$17.80/AUM



Findings: Mr. Lon Waid and Ms. Stacey Waid appeared and presented testimony on behalf of the Lessee. The High Bidder did not make an appearance. This lease is comprised of 640 acres of grazing land located within Section 36, Township 30 North, Range 16 East, in Hill County, Montana. It is approximately 16 miles south-southeast of Havre, Montana in the Bearpaw Mountains at an elevation of approximately 4000 feet above sea level. Abundant Aspen and Douglas Fir trees reflect a precipitation zone of 15 to 19 inches per year. Reliable stock water on this tract is provided by a developed spring and reservoir and a couple of stock tanks. Several drainages within the tract have flowing water within them. There are no roads present on the lease. The Lessees access this tract through their private lands, which lie adjacent to this tract on both the north and east boundaries of the Lease. The Lessees adhere to a light grazing philosophy of "take half and leave half" which has resulted in excellent range conditions on this tract. The Lessees have attempted to vary the date of use on this tract so as to promote good vigor and production of grass species. Although much of the topography of this tract is steep and brushy, the Lessee has achieved good livestock distribution with salting. This tract experiences little recreational use. The Lessee has seen some Hound's-tongue weeds on this tract, but the Lessee has effectively controlled those noxious weeds by applying herbicide with a four-wheeler.

No evidence was provided in the hearing to show that the High Bid of \$16.94/AUM was either economically or biologically viable for similar tracts of grazing lands, while adhering to good range management practices.

Recommendation:

I recommend that the Board issue the next ten-year term of Lease No. 3121 to Lon & Stacey Waid at the rate of \$14.00/AUM. The Waids are the best-qualified Lessee as evidenced by their excellent past management of this tract, and the failure of the High Bidder to propose a better range management plan. The Lessee's past stewardship of this tract is commendable.

This tract represents one of the more-productive state grazing leases in Hill County. The water and forage available on this tract is greater than that possessed by the average grazing tract in Hill County. However, the lack of roads and steep topography provide management challenges. The value of this tract is somewhat more than the DNRC County Competitive Bid Average for Hill County, but somewhat less than the Agricultural Statistics Survey state-wide rental value for 2007. Therefore, I find that \$14.00/AUM, best reflects the prevailing community standard for this lease.